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FINAL REPORT

PROVINCIAL FARM DEBT REVIEW BOARD

December 1986

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1. BACKGROUND

During the course of its deliberations on behalf of financially-troubled farm operators, the provincial Farm Debt Review Board (F.D.R.B.) was exposed to a cross-section of the financial problems facing the Island farm community. Although the financial needs of these operators were urgent, in many instances the F.D.R.B. could offer only moral support and perhaps a brief respite from the difficulties facing the individual farmer. Certainly this type of assistance and support is critical to the financially-troubled farm operator and his family; however, in terms of tangible assistance, there was little the F.D.R.B. could do. In some instances "stays of execution" were negotiated with major financial creditors and/or farm supply creditors. In other instances, assistance was given in preparing financial applications or information for the Land Development Corporation (L.D.C.), the Prince Edward Island Lending Authority (P.L.A.), chartered banks and Farm Credit Corporation (F.C.C.). As well, assistance was provided in preparing informal proposals to creditors and in one instance, consultations were provided regarding initiating bankruptcy proceedings. Regardless of the degree of success (or failure) achieved by the F.D.R.B. in its short existence, one fact became increasingly clear to the Board members. That is; the attempted or offered solutions (e.g. provision of operating credit, debt re-structuring, etc.) were mere band-aids in most cases. The root causes of the financial problems were not and perhaps could not be dealt with within the existing farm financial infra-structure. In order to better understand the present

situation and assist in identifying possible solutions to some of these problems, it is first necessary to identify, at least in general terms, the most significant problems facing the agricultural sector.

(a) Farm Income and Commodity Price Levels

Most submissions to Government on behalf of farm organizations (e.g. Federation of Agriculture, N.F.U., etc) identify low commodity prices as a major deterrent to the creation and maintenance of economically viable farm units. Low and often erratic levels of commodity prices, particularly in commodities where supply is not "managed", have been a major contributing factor leading to deteriorating farm incomes and, consequently, deteriorating equity positions for the farmer. A wide variety of subsidy programs, both in other provincial jurisdictions and internationally, further complicate the problem. Debt servicing problems often arise as a direct result of low or sometimes wildly fluctuating income and cash flow levels.

(b) Farm Incomes and Input Cost Levels

In real terms, input costs are rising and commodity prices are falling for many farm commodities. Unless the farmer is able to compensate by means of greater production efficiencies, he is caught in a vicious cost-price squeeze which leads inevitably to lowered

farm incomes, thus reducing equity positions and creating debt-servicing problems.

This is particularly evident in the potato sector. For example, in 1971 the average potato income per hundredweight was $1.42, and that represented a poor year, for in 1969 the average price was $2.01 and in 1972 it was $3.80. For the 1985/86 crop year the average price was $2.66 per cwt., or an increase by a factor of 1.87 over the 1971 price, and considerably less than the 1972 price!

Meanwhile, the cost of many farm inputs has increased at a much faster rate. For example, taking the 1971 costs as being indexed at 100, in 1985, petroleum products were 501.3, pesticides were 425.3 labor was 338.1, non power machinery was 291.5 and fertilizer was 317.5.

Contributing to this problem is the fact that individual farmers are essentially price takers both for the inputs they buy and the products they sell.

(c) Real Cost of Credit

In real terms (that is, adjusted for the inflation factor) interest rates are at all time highs. According to a recent survey by an Ontario Task Force, the real interest rate or cost of credit, between 1970 and 1975, declined from about 5% to a negative factor of -1.4%, thus inducing a tremendous surge in the use of outside credit (instead of equity) to finance expanding farm operations. Between 1975 and 1984, the real cost of credit increased to a previously

unheard of level of approximately 7.7%. As it is a capital intensive business requiring massive amounts of credit, agriculture suffered accordingly. Economic forecasters predict no significant change in the high real cost of credit over the next few years.

(d) Capital Intensive Nature of Agriculture

Rising real estate and equipment costs, increasing size of economic farming units, new technologies in mechanized farming operations and speculative investing in farm lands are but a few of the factors contributing to the capital intensive nature of the farming business. In a nutshell, the entry cost into the business, in terms of capital requirements (land, buildings and equipment), is extremely high and ever-increasing. It is becoming more and more difficult to establish and maintain a sound equity position in a farm operation. As the accumulation of a substantial equity position to enter the business or stay in the business becomes increasingly difficult, farmers turn to debt financing, thus creating highly leveraged (and hence, risky) business structures. This dangerous cycle of high capital requirements is fuelled by the need to expand and purchase new technology in order to remain competitive in production terms. The expansion is financed by shrinking pools of equity capital and ever-increasing pools of debt capital, which in turn exposes the farm operation to greater degrees of risk and substantially increased credit costs. The increased costs in turn are likely to lead to further capital requirements to remain "competitive", thus perpetuating a seemingly endless cycle.

(e) Lack of Equity Sources

Farm operators who do not have a substantial equity position (depending on the type of operation, "substantial" could range between 35 - 60% equity ownership) are constantly exposed to the risk of financial failure precipitated by low commodity prices, natural disasters, crop or livestock disease, high input costs, etc., etc. In short, a large equity ownership portion is necessary to prevent debt-servicing problems which, unless brought under control, inevitably lead to the failure of the farm as a business operation. The question is, "Where does the new farm operator acquire the necessary equity investment?" Retiring farmers, a traditional source of farm equity by way of handing over farm assets to the next generation, are increasingly tending to withdraw their capital as they leave the agricultural sector. Thus the beginning farmer is faced with obtaining a very substantial, and possibly dangerous, proportion of his capital investment requirements by way of debt.

(f) Availability of Credit

The lack of availability of credit on suitable terms and at reasonable cost is in most cases, a problem of considerable importance to the farm operator. In certain instances, the lack of easily available credit has proved to be a blessing in disguise as it sometimes prevented farm operators from acquiring debt loads they could not possibly service over the long run. Credit availability is, in fact, the ultimate two-edged sword. When obtained under acceptable terms and conditions and in good balance and proportion to

the owners equity position, credit can provide positive leverage and enhanced returns on investment for the farm operator. When obtained in quantities out of proportion with the owners equity position and under unfavourable terms and conditions, it can quickly lead to financial ruin. However, presuming credit to be necessary and economical in the context of this discussion, certain problem areas do exist regarding interest costs, lender's security requirements and the seeming inflexibility of lenders (particularly Government sponsored agencies) on negotiated settlements, write-downs and/or re-writing loans to include interest and principal arrears. In fairness, this "inflexibility" of Government agencies as lenders often relates directly to the regulations governing the agency in question rather than the responsible individuals within the various agencies.

(g) Farm Management Skills

In general terms, there is little doubt that the development of farm management skills has not kept pace with the rapidly expanding size and complexity of the farm business unit or the increasing need for up-to-date financial information for the benefit of creditors and investors and for day-to-day farm management. While there are certainly many bona-fide exceptions to this generalization, there exists a significant proportion who, despite heated denials in some instances, are in fact quite deficient in the management skills necessary to operate farm units which often employ total assets exceeding one million dollars. The management skills referred to include both financial skills and production skills. As an example,

it is almot unheard of for a retail business (employing assets of, say $500,000) to not have monthly financial statements prepared on an accrual basis. Conversely, it is almost unheard of for the farm operator (employing assets of, say $500,000) to have montly financial statements on the accrual basis. In fact, his annual statements, often prepared for the sole benefit of Revenue Canada, are frequently prepared on the cash basis rather than the more informative accrual basis. It may even be fair to surmise that, were it not for the insistence of Renenue Canada or their banker, a significant number of farmers would not even bother to prepare financial statements, production records and the like. This is a rather deplorable situation considering the availability of assistance in such matters from both the agri-government sector and the professional sector. On the other side of the coin, it is often true that the skills and services provided by the professional sector and, in some cases, the agri-government sector simply do not meet the needs of the farm operator. This situation could be improved if all lenders were to spell out explicity in the credit agreement that the farmer was to provide appropriate financial statements (e.g. accrual income statements and a balance sheet on an annual basis).

(h) The Concept of Farm Debt Review Boards

Considerable uncertainity and doubt continues to surround the concept of third party debt review. Prince Edward Island has experienced both a provincial farm debt review board which operated essentially without powers and more recently, a federal farm debt review board which has significantly more power than its provincial

counterpart. As well, the federal board has the moral suasion of federal legislative intent. Although both of these entities have (or has) been in operation for a very short time, there is considerable controversy over their effectiveness. Proponents of debt review boards maintain that the existence of such boards shifts the balance of power away from lenders (presumed to be sophisticated in financial matters) to the borrowers, with the objectives of preventing the loss of potentially successful farmers from the industry and encouraging equity in resolving lender/borrower disputes by assuring the borrower gets due process.

While the present federal farm debt review board does not have the power to impose its decisions on lenders, there nonetheless appears to be a great deal of resistance to the review board concept from the financial community. Lenders resent the interference with normal collection and security realization methods available to them as part of their contractual agreements with borrowers. Many lenders point out that, in the past, concessions were often negotiated between borrowers and lenders without the impetus of debt review boards. Other lenders categorically state that the existance of a debt review board with powers to interfere in the collection process will lead them to cut off some of the more risky loans now being made. This would inevitable lead to more public participation in the area of high risk loans through government lending agencies.

Not only lenders are concerned. Some successful farmers have strong reservations on the concept and existence of debt review

boards. They foresee situations where poor farm managers may receive assistance to stay in business while the better managers are not rewarded in any way and in fact end up subsidizing poorer farm managers. They also point to the possibility of credit sources now available to them drying up or borrowing becoming more costly as a result of lenders not being willing to tolerate the interference and uncertainty created by debt review boards.

We are aware of a number of successfully negotiated settlements achieved between borrowers and lenders (or other creditors) prior to the existence of debt review boards. These negotiated settlements all appear to have one feature in common. In every instance, all parties believed they were better off in monetary terms by reaching a compromise settlement than they would have been had foreclosure and/or bankruptcy occurred. In our view, debt review boards can only hope to have a measure of success if they act in such a manner as to provide equity to both borrowers and lenders by assuring all parties to a settlement are better off, in monetary terms, than they would have been in foreclosure and/or bankruptcy.

2. EXECUTIVE SUMMARY

Background:

The specific services required by the farming industry in dealing with the debt crisis far exceeds that which offered by a debt review board. Significant problem areas would include low and erratic commodity prices, rising input costs, a record high real cost of credit, the high capital requirements of farming, lack of equity capital, the availability of credit under appropriate terms and conditions, and farm management skills that are not appropriate to the size and complexity of many farms.

The situations where farm debt review boards can make significant contributions will be those where the board is instrumental in the identification of a settlement which leaves all parties at least no worse off then they were prior to intervention and some parties significantly better off.

Board Activities:

Twelve farm cases representing eighteen farm families were dealt with by the board. Nine of the cases had potato enterprises, while three had dairy enterprises and one was a specialized tobacco operation. Board activities included specific recommendations to the farmers in regards to debt restructuring, preparation of credit proposals, and the keeping and use of financial and production

records.

In several cases, letters were provided to lending agencies supporting proposals put forward by the farmer.

Present Farm Financial Situation

Statistics on the present farm financial situation were gathered from a variety of lenders. Generally, excellent co-operation was received by public sector lenders and some private sector lenders. Other private sector lenders, for various reasons, contributed less.

The potato sector, as expected, is the one most deeply affected by the present crisis. However, it is also the sector that is most likely to benefit from a large price increase for its product. The lack of hard data on the present equity and per acre debt situation of those in arrears precludes any accurate prediction of the effect the anticipated strong market price will have on the many farms in arrears. However, it is certain that one year of high prices will allow some farmers to bring all arrears up to date. For others, while the situation will improve,they will remain in a very precarious financial situation.

There were a surprising number of dairy farms in arrears. In a supply managed commodity, this is a cause for some concern. Some of these problems are carryovers from the quota crisis of four years ago, while others are directly related to the management skills of the farmer.

Except for the Farm Credit Corporation, the number of swine loans in arrears was surprisingly low. There were a number of tobacco farms with serious arrears problems.

Observations on Credit Institutions:

Problems with the appeal systems in place in the P.E.I. Lending Authority, and the Land Development Corporation were identified; i.e. the appeal is made to the same group that made or ratified the original decision; the appeal hearing may be needlessly intimidating for the farmer; and the decision making body has a very limited time in which to discuss the case.

If high risk lending is required of government agencies, than the agencies have to be given the mandate and the funds to carry out this role.

The Farm Credit Corporation does some research into the area of farm financing.

Private banking institutions, farm suppliers who deal on a credit basis, and private individuals all play an important role in the farm finance area.

Farm Finance Programs and Policies in Canada:

Interest rebate programs are found in almost all provinces, and the federal government is involved through some Farm Credit Corporation programs. Most programs are aimed at reducing the interest cost on term loans, although there are a few programs to subsidize operating loans.

Most jurisdictions offer loan guarantees of some type, although such programs are recognized as being potentially difficult to administer. Most grant programs that are in place are commodity specific. The three Maritime provinces each operate a land leasing program, while five provinces offer programs aimed specifically at new farmers.

In addition to the federal and Prince Edward Island debt review boards, Manitoba and Saskatchewan have set up debt review procedures. Manitoba had a board with no powers for several years. It was used very little by farmers, and is being replaced by a much more structured board that relies heavily on the court process.

Saskatchewan's Farm Land Security Act puts a moritorium on the sale of any farm land, as well, a panel review process is provided under the Farmer's Counselling and Assistance Act.

Recommendations:

(1) Government intiate discussions with the Canadian Bankers Association to put in place a mechanism which will provide government on a regular basis, data suitable and necessary for policy monitoring and development.

(2) The appeal procedure within the P.E.I. Lending Authority and the Land Development Corporation be adjusted so as to provide a more in depth study of each case by a subcommittee of the board.

(3) That government provide a fund to enable the P.E.I. Lending Authority to make high risk loans to individuals who would not qualify under their normal lending mandate, but who can exhibit a reasonable ability to operate a viable farm.

(4) When new P.E.I. Lending Authority staff are being recruited, consideration should be given to hiring individuals with agricultural backgrounds and/or education.

(5) It is recommended that the Land Development Corporation be empowered to consider purchasing land and leasing it back to the same individual with an option to purchase.

(6) It is recommended that the provincial government strongly

encourage continued and expanded research in the area of farm finance by the federal government and the Farm Credit Corporation.

(7) It is recommended that the provincial government strongly encourage all lending institutions, and in particular the chartered banks, to staff appropriate positions in the branches with individuals who are experienced and well trained in agricultural production and lending.

4. PRESENT FARM FINANCIAL SITUATION

The commentary in this section was developed from information supplied by the major lenders in the province. Excellant co-operation was received by the government agencies and by a credit union which is very active in the agricultural lending field. In some cases, provision of the requested information required a significant investment of time by staff of the credit agency.

The chartered banks were less than enthusiastic and in fact did not provide any factual information. There are several reasons for this:

(1) There would have been a significant cost to them to collect information that was requested from the individual branches. The banks are not computerized to the extent that aggregate data by

commodity, equity level, etc. can be extracted from a computer data base. The information would have had to have been collected manually by going through individual files

(2) Some of the bank personnel were very sympathetic to what we were doing, while others viewed us with some suspicion. In retrospect, it would have been better to have approached them through the local Canadian Bankers Association rather than on an individual basis. Nevertheless, the end result would likely have been the same.

(3) There is a natural concern about confidentiality of data and market share.

(4) It was felt by some bankers that the data they could supply would not be of much use to us because of the time of the year; the picture in regards to their loans would be much clearer in April when the potato marketing season is nearly complete.

The ideal situation would be to have a standing agreement with the Canadian Bankers Association to provide aggregate information to government for policy monitoring and development purposes on a regular basis. It is recommended that government initiate discussions with the Canadian Bankers Association towards this end. As banks move more fully into the computer age, this data will become

easier to collect. However, it must be recognized that there will be a cost in collecting this data, and government should be prepared to aid in bearing that cost.

The general financial outlook has improved significantly over the past four months. The market outlook for potatoes, and hog prices well over the stabilization level, have contributed to a much happier outlook.

However, the problem has not gone away. There are still a significant number of farms with severe financial problems.

Farm Credit Corporation

The Farm Credit Corporation figures were as of September 1, 1986. The length of time in arrears is calculated by dividing the total outstanding by the annual payment. There were 275 loans in arrears at that time. The potato enterprise had the highest number of arrears both in numbers (133) and as a percent of outstanding loans for that commodity (48.7%). The amount of arrears outstanding ($2.78 million) was 129% of the annual installment due for the commodity. The dairy industry had the second highest number of loans in arrears (51), and while that represented only 16.3% of the outstanding dairy loans, it could be a cause for concern that some 40 farms in this commodity would not be up to date with their payments. However the arrears outstanding per loan in arrears was the lowest of any commodity ($7,690). The pork industry arrears were spread over

47 loans, which represented 35.9% of the swine commodity loans. However, the average amount of arrears was low ($7,871). The other notable fact in the figures was that 15 tobacco loans were in

arrears, and while that only represented 22% of the outstanding tobacco loans, the average amount of arrears was $23,005. Potatoes, by comparison, had an average arrears of $20,919. The total outstanding arrears was $4.138 million, and the potato arrears represented 67% of this. The loans over one year in arrears totalled 175 or 63% of all loans in arrears. In summary then, the figures illustrate that the problem is greatest in the potato industry. However, the large number of dairy producers that are having some problems is of concern, as is the high average level of arrears by a few tobacco producers.

P.E.I. Lending Authority

Because the P.E.I. Lending Authority provides both operating and term loans, it was difficult to determine an exact number of farms that would be considered a severe problem (loans more than one year in arrears and with owners equity in the operation at less than 25%). However, the detailed figures provided by the P.E.I. Lending Authority staff do allow us to state that their clients include at least 30 and maybe as many as 41 clients that would be in severe distress as defined above. The potato industry represents the majority of these (24-34 farms) and 89.7% of the total arrears amount. The potato arrears amount to $2.8 million, with 40.4% of potato loans in arrears. The average amount of arrears per loan in this commodity was $26,462. The dairy sector has 3-4 farms in severe trouble, while 14% of the dairy loans were in arrears. The average arrears amount was only $3,160. The swine sector had only two farms more than one year in arrears, and both of these cases were farmers

with 26-50% equity in their farms. The average arrears amount was $3,600 and only 8.7% of the swine loans were in arrears. The tobacco sector had only 3 loans in arrears, one operating and two long term loans, so it is difficult to make generalizations on this commodity.

Land Development Corporation

If we apply the same percentage breakdown to loans more than one year in arrears as to all loans in arrears, then we could assume the following number of "serious" cases.

Potato	32
Dairy	19
Swine	8
Beef	9
Other	15
TOTAL	83

The potato sector has the largest problem; however, it is the most susceptable to improvement from a good price year.
There appears to be a significant problem in the dairy sector. This arises out of the fact that a lot of Land Development Corporation dairy customers are new entrants who got caught short of quota and with an excessive debt load about four to five years ago. Some of the "other" accounts include woods loans. There is not a one-to-one correlation between number of loans and number of farms - so the

number of farms more than one year in arrears may total less than seventy.

Chartered Banks and Credit Unions

One bank representative made the comment that over the next three to four months the picture will become much clearer. The price outlook in some major commodities provides a reason for some optimism. In summary, they do not perceive a crisis now, but realize that the situation can change for the better or worse very rapidly. One credit union with a significant agricultural loan portfolio provided a detailed breakdown of their arrears. The potato sector with 100 loans representing 50 farms had 8% of their loans in arrears, with an average arrears amount of $11,861. None of the loans were over one year in arrears. However, the lack of any operating in arrears may indicate that operating loan carryovers from 1985 were rolled into term loans. The dairy sector had 7 loans in arrears, one of which was more than one year in arrears. The average arrears amount was $4,294. The swine accounts were few in number, but did not indicate any arrears. The beef sector had 5 loans from 3 farms in arrears. The average amount of arrears was $8,312, although none were more than one year in arrears.

5. OBSERVATIONS ON CREDIT INSTITUTIONS

P.E.I. Lending Authority

Procedures - Applications are handled by field staff under the

direction of loans officers. Applications for amounts over $100,000 have to be approved by the Board of Directors made up of representatives of Agricultural, Fisheries and Tourism, and Small Business sectors, both private and government. Appeals of decisions by either staff or Board are made to the Board. Information on a case is presented to the Board, in summary form, by means of

overheads. Standard financial data is presented, and a recommendation from staff is provided. Following discussion, a decision is rendered by means of a vote. Appeal procedures are similiar, except that in addition, the applicant is provided with an opportunity to make a presentation to the Board on the merits of his case. Some of the perceived problems with this system are as follows: (1) The appeal is usually being made to the same group that made the original decision. To some extent, this can be justified by the fact that the appeal must be based on information that was not available to the Board for the original decision. In practice, though the new information is often marginal in nature, the most important difference lies in the fact that the Board members meet the applicant in person and thus have an opportunity to assess for themselves the intangible but important factors of personality, attitude, potential for management ability, etc.; (2) The appeal

hearing can be a very intimidating event for the applicant; the Board and staff members present total about fifteen people. To be called upon to make a relatively short presentation to such a large group, most of them stangers, knowing that the effectiveness of your presentation will affect their decision and thus your future, would

be indeed frightening to almost anyone. Indeed, it is felt by the Farm Debt Review Board that this was a severe problem for one of our clients;

(3) The Board members have little opportunity to make detailed study of the applicant's submission or the staff's analysis and recommendations. There just isn't enough time.

Recommendation:

That the appeal procedure be adjusted as follows:

(1) That a separate appeal group be set up consisting of three board members. Following a decline by staff or the Board, the farmer has fifteen days to launch an appeal. Prior to the appeal date, the following responsibilities must be met.

- The P.E.I. Lending Authority staff must provide the appeal group members with copies of all documentation provided to the P.E.I. Lending Authority by the applicant, along with staff analysis and comments. (The analysis and comments would not be available to the applicant).

- The applicant must provide any new or updated information not in the original application to the appeal group.

- The appeal group must visit the farm.

- During the appeal, the staff and the applicant each make a presentation to the appeal group and are allowed to question each other.

- The staff and the applicant are then allowed to make oral comments to the group with the other party not present, and then the appeal group meets on their own to develop a recommendation to the P.E.I. Lending Authority Board.

- The Board must have the final authority, but it would be expected to follow the direction of the appeal group.

This procedure would be somewhat more costly than the present procedure, however it would address the problems previously listed.

Mandate - Although the P.E.I. Lending Authority may be perceived by many as a "Lender of last resort" that mandate is not specifically given to the authority by the Lending Authority Act or the regulations to that act. Indeed the P.E.I. Lending Authority limits its capital loans to a maximum of 75% of the appraised value of the security provided. If the P.E.I. Lending Authority is to be expected to make relatively high risk loans, it must be given the mandate to do so, and it must be given the money to deal with the losses that will inevitably result.

Recommendation - That government provide a fund to enable the P.E.I.Lending Authority to make high risk loans to individuals who wouldnot qualify under their normal lending mandate, but who can

exhibit a reasonable ability to operate a viable farm. In other words, for good farmers who have had bad luck.

Advantages - 1) would provide a lender of last resort for some cases where good farmers might otherwise be forced to leave the industry.

- 2) would provide an extra degree of lending flexibility to the P.E.I.Lending Authority.

Cost - fund which would be to cover losses on loans only should be at least $500,000.

Administration - would be only for loans specified as high risk in advance by the P.E.I. Lending Authority.
- would be open only for applicants recommended by their appeal group.
- loans would be only for current year operating.
- fund is a reserve for actual write-offs.
- program would not be widely publicized to prevent abuse.
- should be an add on feature that farms under this provision be required to submit financial statements on accrual basis. Fund could provide $500 the first year and $250 the second year to off-set the cost of preparing accrual statements.

<u>Personnel</u> - Present staff are drawn from a variety of backgrounds,

many with banking or credit experience. When new staff are being recruited, consideration should be given to hiring individuals with agricultural backgrounds and/or education, and training them in the credit field rather than vice versa.

The Farm Debt Review Board in its dealings with clients heard a disturbing number of comments about arrogance and rudeness on the part of two or three staff members. Personality conflicts do happen from time to time, and could be particularly expected with clients who are under a lot of stress. It must be recognized that staff were also under particularly heavy stress during the early months of 1986 because of the general agricultural situation. However, whatever the reason, all clients should be treated with courtesy and respect even if they appear not to deserve it. To do otherwise creates a lot of needless problems, as well as an image problem for the P.E.I. Lending Authority.

Land Development Corporation

Procedrues: Procedures are very sililar to those outlined for the P.E.I. Lending Authority. The primary difference is in the size of the Board. Board membership is made up of three farmers and four from government, including an ex-officio member from the Farm Credit Corporation. Consequently the same concerns outlined for the P.E.I. Lending Authority procedures apply to the Land Development Corporation. To deal with those concerns, it is recommended that an appeal body be set up with similar responsibilities and mandate.

Mandate - The mandate of the Land Development Corporation is to act as an agent to purchase land and lease it to farmers with an option

to purchase. Presently, the Land Development Corporation cannot purchase land from a farmer and lease it back to the same farmer.

RECOMMENDATION:

That in cases so recommended by the Federal Farm Debt Review Board, the Land Development Corporation be empowered to consider purchasing land and leasing it back to the same individual with an option to purchase at the end of five years.

Government to provide funds, through the Land Development Corporation, to allow farmers to arrange sale and lease-back of farm real estate, at fair market value, with an option to re-purchase at same price within five years. The program would be restricted to farmers exhibiting good farm management skills (both financial and production).

Areas of Concentration - Concentrate on those farms which still have relatively good equity positions and good farm management in place, but have a severe liquidity problem stemming from unpaid short and intermediate term creditors from last crop year. An example might be the farmer who has $50-$100,000 unpaid short term credit from a previous year, but who has equity of perhaps $150-$200,000 in farm land at fair market value.

Suggested Incentive - Government lease-back property at normal Land Develoment Corporation interest plus 2% over-ride. This excess could

be held in special reserve fund which would build up over a five year period and become available to the farmer to apply as a partial down-payment on re-purchase of the land. The reserve plus the option to re-purchase at fixed price would give the farmer a good deal of incentive to operate productively and build equity in order to be eligible to receive the reserve and have the ability to finance the re-purchase with a conventional lender such as the Farm Credit Corporation, P.E.I.Lending Authority , etc.

Cost - Extra costs would be administrative only, plus some extra risk factor from declining land values.

Farm Credit Corporation

Procedures - Applications are handled by local staff who have limited approval authority. All other cases are approved or declined by staff in the regional office in Moncton. Local staff make recommendations on these cases. Appeals are dealt with by a three person appeal board made up of farmers, who make a recommendation to the regional office. The recommendations are almost invariably followed. The cost of the appeal procedure is about $3,000 per case, including staff time and travel from Moncton for the appeal.

Mandate - Mandate is to provide long term credit. Farm Credit Corporation staff are actively researching alternative financing methods and have introduced concepts such as Commodity Based Loans and Shared Risk Mortgages. While the latter program has not been widely used, the Commodity Based Loans do hold some promise.

Recommendation - The provincial government strongly encourage continued research in the area of farm finance by the federal government and Farm Credit Corporation. In particular, forms of equity financing, as opposed to debt financing, should be vigorously investigated.

Chartered Banks and Credit Unions

While most, if not all of our clients relied to some extent on banks for intermediate and operating capital, the Farm Debt Review Board had little contact with banks over these specific cases. One aspect that has emerged is that the service that a farmer gets from a specific bank is very much a function of the background and interest of the local manager or agricultural loans officer. Where the bank officer is experienced in working with agricultural accounts and familiar with agricultural production methods, the service can be very good. On the other hand, where the officer is unfamiliar with and inexperienced in dealing with agricultural enterprises, the situation becomes time consuming, frustrating and potentially expensive for the farming client. Individual clients should not have to bear the sole responsibility for training bank employees. In many, but not all, cases, that is the present situation, as new employees learn about agricultural loans on the job. The Farm Debt Review Board recommends that government strongly encourage chartered banks and indeed, all lending institutions to staff appropriate positions in the branches with individuals who are experienced and well trained in agricultural production and lending; and further, that a definite program of training be provided for bank employees

likely to be promoted to such positions.

Other Sources of Credit

Other sources of agricultural credit are trade credit and loans from private individuals. Credit provided by agri-business firms to farmers has become very important to farmers, and indeed for some individuals it has been the only source of operating credit for the last two cropping seasons. The problem with this type of credit is two fold; firstly it is very expensive. A monthly rate of 2% compounded monthly converts to an effective annual rate of 26.8% while a two and one-half percent per month rate becomes 34.5% per annum. Discounts for prompt payments that are missed would serve to further increase this rate. Secondly, many suppliers of trade credit operate on a very slim margin and are unsecured creditors. In a farm financial crisis, these small local firms are the ones other than the farmers themselves that stand to lose the most. Where the trade credit suppliers are small, locally-based businesses, one significant loss can have wide ranging effects throughout the community.

Private lenders are often family members, and while this credit may be available to a farmer at a very favourable rate, any default in payment can cause a family as well as a financial disaster.

6. FARM FINANCE PROGRAMS AND POLICIES IN CANADA

Credit and farm finance programs offered by the federal government and provincial governments can be classified by the type

of benefit they provide.

Interest Rebates

Interest rebates on term loans are provided by all provinces except Prince Edward Island, and if the Small Business Bond Program and the Farm Credit Corporation Shared Risk Mortgages and Commodity Based Loans are considered as interest subsidization, then the Federal government can also be included. In some cases, the loan funds are offered at a reduced rate by a provincial lending agency; alternatively the subsidy can apply to a loan from any approved lender. A cap is put on the amount of subsidy for any one operation in a variety of ways. A maximum rate of rebate (eg. 3%); a maximum loan amount (eg. $150,000); a stated rate below which a subsidy will not be paid (eg. 8%), a set rate of interest (eg. 12%); and a maximum amount of rebate per year (eg. $10,000) are all used in various combinations to provide this cap.

Some programs are targeted to specific groups, such as young or beginning farmers, or farmers with a high level of debt or for specific purposes such as land improvement. In total, over twenty-five programs were identified across the country.

Subsidies on operating loans are much less common. Advance payment programs, which provide money interest free for a limited period of time are operated by the federal government and by Saskatchewan. Saskatchewan also offers loans for the purchase of feeder cattle at a rate of 12%, which could provide an element of

subsidization if interest rates rose. Newfoundland offers loans on all terms at a rate 3% below prime, while Ontario subsidizes operating loans down to 9 3/4% for high debt farmers.

Loan Guarantees

Most jurisdictions offer loan guarantees. Newfoundland, Nova Scotia, and Prince Edward Island are the only exceptions. The federal involvement is through the advance payment program and the Farm Improvement Loan Program.

In most programs, the maximum rate of the loan is limited to the prime rate plus 1% or 2%. In some cases, the amount of the guarantee is limited to a portion (e.g. 90%) of the outstanding loan. Some programs can be accessed only if the farmer cannot get financing without the guarantee, or if the guarantee is for a specific commodity. Although both operating and term loan guarantees are relatively common, provincial officials have commented that programs such as these can be very difficult to administer, and unless carefully designed, are open to abuse by lenders.

Grants

Most provinces have grants programs which are commodity specific. These programs are designed to expand production or improve management practices in a specified commodity. The Swine Incentive program and the Beef Cos-Calf policy in Prince Edward

Island are examples of these programs.

Newfoundland operates a capital grants program with 50% grant for buildings, equipment and livestock and a 75% grant for land improvements. The maximum grant per farm is $25,000. Manitoba offers a 50% grant of up to $6,000 per year as an interest rate relief for farmers in financial difficulty because of high interest rates.

Land Leasing

The three Maritime provinces each operate a land leasing program. All programs provide a five year lease. Nova Scotia's lease rate is 8%, while New Brunswick offers the lease at $1 per year in years one and two, and at a 5% rate for the last three years.

New Farmers

Five provinces offer programs aimed specifically at new farmers, and all programs are based on an interest rebate. With the exception of Nova Scotia, which offers a rebate of $15,000/year for two years, all the programs reduce the interest for the first five years.

Other Programs

Three provinces have specific legislation in place that allows them to set up ac hoc disaster relief programs.

Ontario operates a Farmers in Transition program for farmers who are being forced off their farm.

The federal government is also operating a similiar program for farmers who have to leave the industry.

Debt Review Boards

In addition to the federal and Prince Edward Island debt review boards, Manitoba and Saskatchewan have set up debt review processes.

The Manitoba legislation sets up a review board. A creditor has to apply to the court for leave to commence action, and also file notice of the application with the board. The board holds an inquiry and presents a report to the court. The court has the power to impose a settlement if one can't be reached by consensus. The act also empowers the Lieutenant Governor in Council to issue a general stay of proceedings on all collection actions. The act also outlines the establishment of peer advisory panels to provide management advice, and an agreement registry to register any agreement arrived at by creditors and farmers.

This legislation has the potential to be very cumbersome.

At the present time, this act has not yet been proclaimed, so is not available for use by farmers.

The province feels that it may have some legislative problems in dealing with security held under Section 178 of the federal Bank Act. Also, it is committed to providing about $6.5 million to facilitate farmer-lender agreements, and the way that this will be used has not been determined. The act will likely be up and running early in 1987.

Manitoba had a board in place for some time which had no powers, and while it provided some useful functions as a conciliator, it was not used extensively by farmers (about thirty cases over a three year period). It was felt that the formal requirements of the present act would lead to a more systematic and timely approach to the problems.

Saskatchewan provides a review process by a panel under the Farmers Counselling and Assistance Act. The process is initiated by the farmer. Upon the recommendation of a panel, the province will provide an operating and/or debt consolidation loan guarantee for up to $200,000.

The Farm Land Security Act puts a moratorium on the sale of any farm land. The only way that a sale can proceed is for the lender to apply to the court for leave to proceed. The burden of proof is on the lender to establish that the farmer has no reasonable possibility of meeting his obligations under the mortgage or that he is not making a sincere and reasonable effort to meet his obligations. Prior to the hearing on a case, a Farm Land Security Board has to provide a written report on the case to the court. Apparently these

acts are not seen as major irritants by creditors, however they may not be doing much more than delaying the inevitable. Both programs are scheduled to end early in 1987, but it would be reasonable to expect that they would be extended.